

commitment and ability to handling financial obligations successfully and ability to make payments on the new mortgage obligation.

(2) Loans acceptance by an Agency approved automated underwriting system eliminates the need for the lender to submit documentation of the credit qualification decision as loan approval requirements will be incorporated in the automated system.

(3) For manually underwritten loans, lenders must submit documentation of the credit qualification decision. Lenders will use credit scores to manually underwrite loan mortgage requests. Lenders are required to validate the credit scores utilized in the underwriting determination. Indicators of significant derogatory credit will require further review and documentation of that review. Indicators of significant derogatory credit include, but are not limited to:

(i) A foreclosure that has been completed in the 36 months prior to application by the applicant.

(ii) A bankruptcy in which debts were discharged within 36 months prior to the date of application by the applicant. Applicants who have completed a bankruptcy debt restructuring plan must have completed the plan and demonstrated a willingness to meet obligations when due for greater than the 12 months prior to the date of application by the applicant.

(iii) One rent or mortgage payment paid 30 or more days late within the last 12 months prior to application by the applicant.

(iv) A previous Agency loan that resulted in a loss to the Government.

(4) When evidence of significant derogatory credit is present, lenders may consider extenuating circumstances, including but not limited to, whether the problems were caused by factors temporary in nature, if the circumstances leading to the derogatory credit were beyond the control of the applicant, and if the loan would significantly reduce the applicant's housing expenses.

(5) In all cases, the applicant cannot have an outstanding Federal judgment, other than a judgment obtained in the United States Tax Court, or a delinquent non-tax Federal debt that has

not been paid in full or otherwise satisfied.

(6) For applicants without an established credit history, alternative methods may be used to evidence an applicant's willingness to pay, such as a non-traditional mortgage credit report or multiple independent verifications of trade references.

(7) A credit report for a non-purchasing spouse must be obtained in order to determine the debt-to-income ratio referenced at §3555.151(h) if the applicant resides in a community property state.

(8) Lenders are encouraged to offer or provide for home ownership counseling. Lenders may require first-time homebuyers to undergo such counseling if it is reasonably available in the local area. When home ownership counseling is provided or sponsored by Rural Development or another Federal agency in the local area, the Lender must require the borrower to successfully complete the course.

(j) *Obtaining credit.* The applicant must be unable to obtain traditional conventional mortgage credit, as defined by the Agency, for the subject loan.

§3555.152 Calculation of income and assets.

The lender must obtain and maintain documentation in the loan file supporting the lender's determination of all income and assets described in this section.

(a) *Repayment income.* Repayment income is the amount of adequate and stable income from all sources that parties to the promissory note are expected to receive. Repayment income is used to determine the applicant's ability to repay a loan.

(1) The lender must examine the applicant's past income record for at least the past 2 years and any applicable training and/or education. The Agency may require additional information and documentation from self-employed applicants and applicants employed by businesses owned by family members.

(2) The lender must establish an applicant's anticipated amount of repayment income and the likelihood of its continuance for at least the next 3

years to determine an applicant's capacity to repay a requested mortgage loan in accordance with § 3555.151(h)(1).

(3) Income may not be used in calculating an applicant's ratios if it is from any source that cannot be verified, is not stable, or is likely not to continue.

(4) The following types of income are examples of income not included in repayment income:

(i) Any student financial aid received by household members for tuition, fees, books, equipment, materials, and transportation;

(ii) Amounts received that are specifically for, or in reimbursement of the cost of medical expenses for any family member;

(iii) Temporary, nonrecurring, or sporadic income (including gifts);

(iv) Lump sum additions to family assets such as inheritances, capital gains, insurance payments and personal or property settlements;

(v) Payments for the care of foster children or adults; and

(vi) Supplemental Nutrition Assistance Program payments.

(b) *Annual income.* Annual income is the income of all household members, regardless of whether they will be parties to the promissory note.

(1) Applicants must provide the income, expense and household information necessary to enable the lender to make income determinations.

(2) Lenders must verify employment and income information provided by the applicant for all household members. Lenders will verify the income for each adult household member for the previous 2 years. Written or oral verifications provided by third-party sources or documents prepared by third-party sources are acceptable. Lenders must project the expected annual income for the next 12 months from the verified sources.

(3) The lender remains responsible for the quality and accuracy of all information used to establish a household's eligibility.

(4) Household income from all sources including, but not limited to, income from temporarily absent household members, allowances for tax-exempt income and net family assets as defined in paragraph (d) of this section

are to be considered in the calculation of annual income.

(5) The following sources of income will not be considered in the calculation of annual income:

(i) Earned income of persons under the age of 18 unless they are an applicant or a spouse of a member of the household;

(ii) Payments received for the care of foster children or foster adults and incomes received by foster children or foster adults who live in the household;

(iii) Amounts granted for, or in reimbursement of, the cost of medical expenses;

(iv) Earnings of each full-time student 18 years of age or older, except the head of household or spouse, that are in excess of any amount determined pursuant to HUD definition of annual income at 24 CFR 5.609(c);

(v) Temporary, nonrecurring, or sporadic income (including gifts);

(vi) Lump sum additions to family assets such as inheritances; capital gains; insurance payments under health, accident, or worker's compensation policies; settlements for personal or property losses; and deferred periodic payments of supplemental social security income and Social Security benefits received in a lump sum;

(vii) Any earned income tax credit;

(viii) Adoption assistance in excess of any amount determined pursuant to HUD's definition of annual income at 24 CFR 5.609(c);

(ix) Amounts received by the family in the form of refunds or rebates under State or local law for property taxes paid on the dwelling;

(x) Amounts paid by a State agency to a family with a developmentally disabled family member living at home to offset the cost of services and equipment needed to keep the developmentally disabled family member at home;

(xi) The full amount of any student financial aid;

(xii) Any other revenue exempted by a Federal statute, a list of which is available from any Rural Development office;

(xiii) Income received by live-in aides, regardless of whether the live-in aide is paid by the family or a social service program;

(ix) Employer-provided fringe benefit packages unless reported as taxable income; and

(x) Amounts received through the Supplemental Nutrition Assistance Program.

(c) *Adjusted annual income.* Adjusted annual income is used to determine program eligibility and is annual income as defined in paragraph (b) of this section, less any of the following verified deductions for which the household is eligible.

(1) A reduction for each family member, except the head of household or spouse, who is under 18 years of age, 18 years of age or older with a disability, or a full-time student, the amount of which will be determined pursuant to HUD definition of adjusted income at 24 CFR 5.611.

(2) A deduction of reasonable expenses for the care of a child 12 years of age or under that:

(i) Enables a family member to work, to actively seek work, or to further a member's education;

(ii) Are not reimbursed or paid by another source; and

(iii) In the case of expenses to enable a family member to work, do not exceed the amount of income, including the value of any health benefits, earned by the family member enabled to work. If the child care provider is a household member, the cost of the children's care cannot be deducted.

(3) A deduction of reasonable expenses related to the care of household members with disabilities that:

(i) Enable a family member or the individual with disabilities to work, to actively seek work, or to further a member's education;

(ii) Are not reimbursed from insurance or another source; and

(iii) Are in excess of 3 percent of the household's annual income and do not exceed the amount of earned income included in annual income by the person who is able to work as a result of the expenses.

(4) For any elderly family, a deduction in the amount determined pursuant to HUD definition of adjusted income at 24 CFR 5.611.

(5) For elderly and disabled families only, a deduction for household medical expenses that are not reimbursed

from insurance or another source and which, in combination with any expenses related to the care of household members with disabilities described in paragraph (c)(3) of this section, are in excess of 3 percent of the household's annual income.

(d) *Net family assets.* For the purpose of computing annual income, the net family assets of all household members must be included in the calculation of annual income. Lenders must document and verify assets of all household members.

(1) Net family assets include, but are not limited to, the actual or imputed income from:

(i) Equity in real property or other capital investments, other than the dwelling or site;

(ii) Cash on hand and funds in savings or checking accounts;

(iii) Amounts in trust accounts that are available to the household;

(iv) Stocks, bonds, and other forms of capital investments that is accessible to the applicant without retiring or terminating employment;

(v) Lump sum receipts such as lottery winnings, capital gains, and inheritances;

(vi) Personal property held as an investment; and

(vii) Any value, in excess of the consideration received, for any business or household assets disposed of for less than fair market value during the 2 years preceding the income determination. The value of assets disposed of for less than fair market value shall not be considered if they were disposed of as a result of foreclosure, bankruptcy, or a divorce or separation settlement.

(2) Net family assets for the purpose of calculating annual income do not include:

(i) Interest in American Indian restricted land;

(ii) Cash on hand which will be used to reduce the amount of the loan;

(iii) The value of necessary items of personal property;

(iv) Assets that are part of the business, trade, or farming operation of any member of the household who is actively engaged in such operation;

(v) Amounts in voluntary retirement plans such as individual retirement accounts (IRAs), 401(k) plans, and Keogh

Rural Housing Service, USDA

§ 3555.202

accounts (except at the time interest assistance is initially granted);

(vi) The value of an irrevocable trust fund or any other trust over which no member of the household has control;

(vii) Cash value of life insurance policies; and

(viii) Other amounts deemed by the Agency not to constitute net family assets.

§§ 3555.153–3555.199 [Reserved]

§ 3555.200 OMB control number.

The report and recordkeeping requirements contained in this subpart are currently with the Office of Management and Budget under review and awaiting approval.

Subpart E—Underwriting the Property

§ 3555.201 Site requirements.

(a) *Rural areas.* Rural Development will only guarantee loans made in rural areas designated as rural by Rural Development. However, if a rural area designation is changed to nonrural:

(1) Existing conditional commitments in the former rural area will be honored;

(2) A supplemental loan may be made in accordance with § 3555.101 in conjunction with a transfer and assumption of a guaranteed loan;

(3) Loan requests where the application and purchase contract was complete prior to the area designation change may be approved; and

(4) REO property sales and transfers with assumption may be processed.

(b) *Site standards.* Sites must be modest and developed in accordance with any standards imposed by a State or local government and must meet all of the following requirements.

(1) The site size must be typical for the area.

(2) The site must not include income-producing land or buildings to be used principally for income-producing purposes. Vacant land without eligible residential improvements, or property used primarily for agriculture, farming or commercial enterprise is ineligible for a loan guarantee.

(3) The site must be contiguous to and have direct access from a street,

road, or driveway. Streets and roads must be hard surfaced or all weather surfaced and legally enforceable arrangements must be in place to ensure that needed maintenance will be provided.

(4) The site must be supported by adequate utilities and water and wastewater disposal systems. Certain water and wastewater systems that are privately-owned may be acceptable if the lender determines that the systems are adequate, safe, compliant with applicable codes and requirements, and the cost or feasibility to connect to a public or community system is not reasonable. Certain community-owned water and wastewater systems may be acceptable if the lender determines that the systems are adequate, safe, and compliance with applicable codes and requirements. The Agency may require inspections on individual, central, or privately-owned and operated water or waste systems.

§ 3555.202 Dwelling requirements.

(a) *New dwellings.* New dwellings must be constructed in accordance with certified plans and specifications, and must meet or exceed the International Energy Conservation Code (IECC) in effect at the time of construction. The lender must obtain and retain evidence of construction costs, inspection reports, certifications, and builder warranties acceptable to Rural Development.

(b) *Existing dwellings.* Existing dwellings are considered to meet the following criteria when inspected and certified as meeting HUD requirements for one-to-four unit dwellings in accordance with Agency guidelines:

(1) Be structurally sound;

(2) Be functionally adequate;

(3) Be in good repair, or to be placed in good repair with loan funds; and

(4) Have adequate and safe electrical, heating, plumbing, water, and wastewater disposal systems.

(c) *Escrow account for exterior or interior development.* This paragraph does not apply if the development is related to a “combination construction and permanent loan” under § 3555.101(c). If a dwelling is complete with the exception of interior or exterior development work, Rural Development may